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In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 897

RUSSELL L. IRISH, d/b/a RUSSELL L. IRISH, INVESTMENTS, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 59-63) is reported at 367 F. 2d 637.[1] The findings and opinion of the Securities and Exchange Commission

[1] References to the Appendix of the Petition for a Writ of Certiorari are cited "Pet. App." References to the 14 volume record below, which petitioner has filed with the Court, are cited "R."

(Securities Exchange Act Release No. 7687), dated August 27, 1965 (Pet. App. 39-55), are unreported.

JURISDICTION

The judgment of the court of appeals denying a petition for rehearing was entered on November 25, 1966. The petition for a writ of certiorari was filed on December 22, 1966. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether the findings of the Securities and Exchange Commission of wilful violations of the securities laws by petitioner were supported by substantial evidence.

2. Whether petitioner's rights were violated by the revocation of his registration as a broker and dealer in securities where, although there was a four-year interval between the conclusion of the evidentiary hearings and the scheduling of proposed findings and briefs, petitioner never sought to expedite the proceedings, contributed substantially to the delay, and has shown no prejudice resulting therefrom.

STATUTES INVOLVED

The relevant provisions of the Securities Act of 1933, 48 Stat. 74, as amended, 15 U.S.C. 77a, *et seq.*, the Securities Exchange Act of 1934, 48 Stat. 881, as amended, 15 U.S.C. 78a, *et seq.*, and Rules under the Securities Exchange Act of 1934, 17 CFR 240.0-1, *et seq.*, are set forth in the Appendix, *infra*, pp. 12-16.

STATEMENT

On August 27, 1965, the Securities and Exchange Commission issued its findings, opinion and order (Pet. App. 39-55), pursuant to Sections 15(b) and 15A of the Securities Exchange Act of 1934, 15 U.S.C. 78*o*(b) and 78*o*-3, revoking petitioner's registration as a broker and dealer in securities and expelling him from membership in the National Association of Securities Dealers, Inc. ("NASD") (Pet. App. 54-55). The Commission found that petitioner had violated the antifraud provisions of the federal securities laws[2] in that (1) petitioner had "churned" customers' accounts (*i.e.*, engaged in unwarranted buying and selling in order to increase commissions) by "switching" customers from one mutual fund to another (Pet. App. 42-48);[3] (2) petitioner had purchased mutual fund shares for customers in amounts just under minimum "break points" (Pet. App. 49-51);[4] and (3) petitioner had

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[2] Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q (a); Sections 10(b) and 15(c)(1) of the Securities Exchange Act, 15 U.S.C. 78j(b) and 78*o*(c)(1), and Rules 10b-5 and 15c 1-2 thereunder, 17 CFR 240.10b-5 and 15c 1-2.

[3] "Switching" is the term usually applied to the churning of customers' accounts where mutual fund shares are involved. For a description of "churning" see *Norris & Hirshberg, Inc.* v. *Securities and Exchange Commission*, 177 F. 2d 228, 232 (C.A. D.C.). See also *Report of Special Study of Securities Markets of the Securities and Exchange Commission*, H.R. Doc. 95, 88th Cong., 1st Sess., Pt. 4 at p. 151 (1963).

[4] "Break points" are the quantities at which quantity discounts as to sales charges became available to purchasers of mutual fund shares. For example, in one of the funds here

effected sales of mutual fund shares to two customers at prices in excess of the public offering price (Pet. App. 48). These findings of fact, characterized by the court of appeals as the advancement of petitioner's "own interests to the detriment of his customers," (Pet. App. 60) were in accord with the findings in the hearing examiner's Recommended Decision (Pet. App. 34) and were held by the court of appeals to be supported by substantial evidence (Pet. App. 60).

The court of appeals also rejected petitioner's contentions that certain delays in the proceeding had violated the Commission's Rules of Practice and the Administrative Procedure Act and had deprived petitioner of due process of law (Pet. App. 60-63). The court noted that private proceedings had been commenced on March 19, 1959, and that hearings had been held on four days beginning September 21, 1959. It found that the "evidence at the hearing covered the years 1950 through 1958 and together with the documentary evidence showed serious, wilful misconduct" (Pet. App. 60).[5] It also

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involved on purchases of shares from $1 to $24,999 the purchaser pays an 8½% sales charge, which includes a commission to the dealer of 6%; on purchases from $25,000 to $49,999 the sales charge is reduced to 4%. Prospectus of National Securities Series of July 27, 1953, Commission Public File No. 2-10347-1.

[5] Petitioner states (Pet. 13) that the "instant proceedings covered a period from 1941 to the time of the 1959 hearing." The earliest transaction analyzed by the Commission, however, was in 1950 (Pet. App. 49) and with respect to the

noted, "Between December 3, 1959, and April 5, 1961, several depositions were taken and filed, by stipulation" (Pet. App. 60). The court did not point out, as the Commission did (Pet. App. 52), that between April 1961 and October 1963 the parties engaged in extensive but unfruitful negotiations on a variety of questions. In October 1963 the Commission's Division of Trading and Markets moved to reconvene the hearing to introduce certain exhibits and to have the hearing examiner prescribe a time schedule for the filing of proposed findings and briefs. Not until that motion was denied by the hearing examiner on the grounds of laches and lack of due process did the petitioner move to dismiss the proceeding (Pet. App. 52; R. 1161).

The court below noted that the "succeeding months [following the motion to reconvene] saw motions, briefs, and arguments placed before the Commission, and a petition for review before this court (which this court dismissed)" (Pet. App. 61). By order dated December 12, 1963, the Commission overruled the hearing examiner, denied petitioner's motion to dismiss the charges, determined that the proceeding be deemed closed, and directed that, as preparatory steps to the filing of a recommended decision by the hearing examiner, the parties should file proposed findings and supporting briefs (R. 1162). Petitioner had never requested the hearing examiner to schedule the filing of proposed findings and briefs (R. 1159; Pet. App. 52).

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churning violations the Commission only analyzed the period 1953-1958 (Pet. App. 42).

ARGUMENT

The court of appeals' affirmance of the Commission's order was clearly correct, and the petition presents no question warranting further review.

1. Both the hearing examiner and the Commission found that petitioner had engaged in willful violations of the antifraud provisions of the federal securities laws. The court below held that these findings were supported by substantial evidence. Petitioner nevertheless urges (Pet. 3, 13) that the determination of the court below was erroneous in light of the hearing examiner's statement in his recommended decision that he was at a disadvantage in evaluating the credibility of witnesses because of the delay in the proceeding (Pet. App. 25). The Commission noted, however, that it did not "consider the credibility of witnesses to be a controlling factor" in light of "the importance of documentary evidence in the record," even accepting the testimony of investor-witnesses who were "generally sympathetic" to petitioner (Pet. App. 51, n. 15).[6]

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[6] Petitioner is mistaken in suggesting (Pet. 13) that proof of "evil intent" is required to establish willfulness in a proceeding to determine whether the registration of a broker and dealer should be revoked. *Tager* v. *Securities and Exchange Commission*, 344 F. 2d 5, 8 (C.A. 2); *Gilligan, Will & Co.* v. *Securities and Exchange Commission*, 267 F. 2d 461, 468 (C.A. 2), certiorari denied, 361 U.S. 896; *Norris & Hirshberg, Inc.* v. *Securities and Exchange Commission*, 177 F. 2d 228 (C.A.D.C.); *Hughes* v. *Securities and Exchange Commission*, 174 F. 2d 969, 977 (C.A.D.C.).

Petitioner is also mistaken in contending (Pet. 13) that

Furthermore, the hearing examiner stated that he was "convinced by a preponderance of the evidence" that the violations occurred (Pet. App. 34). The disagreement between the hearing examiner and the Commission related to the remedy—*i.e.*, whether petitioner's registration should be revoked. The hearing examiner believed that revocation was not in the public interest in light of the delays in the proceeding and because, in the absence of contrary evidence in the record, he presumed that petitioner had "mended his ways" since the close of the hearings in 1959 (Pet. App. 35-36). The Commission found (1) that, considering the privacy of the proceedings, petitioner had not been "prejudiced by the delay" to which he had contributed, and (2) that he was not entitled to any presumption of good conduct in view of the nature of his violations and the fact that he had previously been found to have committed similar violations in an earlier proceeding before the NASD involving churning violations in the years 1943 to 1954 (Pet. App. 52-53). The Commission concluded that "the public interest requires the imposition of a sanction" (Pet. App. 54). The appropriateness of

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revocation proceedings are quasi-criminal. Such proceedings have been uniformly held to be remedial and not penal. See *e.g.*, *Tager* v. *Securities and Exchange Commission*, 344 F. 2d 5, 8-9 (C.A. 2); *Berko* v. *Securities and Exchange Commission*, 316 F. 2d 137, 141 (C.A. 2); *Blaise D'Antoni & Associates, Inc.* v. *Securities and Exchange Commission*, 289 F. 2d 276 (C.A. 5); *Pierce* v. *Securities and Exchange Commission*, 239 F. 2d 160, 163 (C.A. 9); *Wright* v. *Securities and Exchange Commission*, 112 F. 2d 89, 94 (C.A. 2).

the remedy in terms of the public interest is, of course, a policy determination within the Commission's discretion which should be disturbed only if it "lacks any rational and statutory foundation." *Securities and Exchange Commission* v. *Chenery Corp.*, 332 U.S. 194, 207. See also *American Power and Light Co.* v. *Securities and Exchange Commission*, 329 U.S. 90, 112-113. Cf. *Federal Communications Commission* v. *Allentown Broadcasting Co.*, 349 U.S. 358, 364.

2. Petitioner contends that the delay in the proceeding violated Section 10(e) of the Administrative Procedure Act (5 U.S.C. 1009(e), subsequently recodified as 5 U.S.C. 706), which authorizes a reviewing court to compel agency action "unreasonably delayed," and deprived him of due process of law (Pet. 2-5, 10, 12). As the court below held, however, petitioner "failed completely to show how the Commission caused him prejudice by waiting until 1965 to revoke his registration" (Pet. App. 62). Indeed, petitioner "did not contest the Commission's delay until the Commission moved (on October 14, 1963), to reconvene the hearing." Citing Sections 6(a) and 10(e), of the Administrative Procedure Act (5 U.S.C. 1005(a) and 1009(e), subsequently recodified as 5 U.S.C. 555(b) and 706), the court pointed out that, although petitioner "could have earlier petitioned a court to compel the Commission to expedite its proceeding," he did not do so (Pet. App. 62-63). Further, as the Commission found, the proceedings were private, petitioner was not prevented from doing

business during the pendency of the proceeding, he offered no proof of financial hardship and he contributed to the delay (Pet. App. 52-53). Cf. *Costello* v. *United States*, 365 U.S. 265, 281-284.

Petitioner's subsidiary contention that due process was denied because the Commission violated its own rules is also without merit, as the court of appeals found. The Commission held that Rule 13 of the Commission's Rules of Practice, 17 CFR 201.13, governing adjournments of hearings,[7] did not apply because it "was not adopted by the Commission until after the hearing was closed in 1959 subject to the filing of depositions, and no adjournment was ordered by the Hearing Examiner following the filing of the last deposition in April 1961, when such limitation was in effect" (R. 1162).[8]

Similarly, Rule 16(e) of the Commission's Rules of Practice, 17 CFR 201.16(e),[9] providing for the scheduling of proposed findings and briefs, did not become effective until October 1, 1960,[10] after the evidentiary hearing had been closed. At no time did petitioner request the hearing examiner to schedule the filing of proposed findings and conclusions.

---

[7] The text of Rule 13 is set forth at Pet. 6-7.

[8] Rule 13 was adopted as a part of a general revision of the Commission's Rules of Practice and did not become effective until October 1, 1960, 25 Fed. Reg. 6719, 6732.

[9] The text of Rule 16(e) is set forth at pages 5-6 of the Petition.

[10] 25 Fed. Reg. 6719, 6733 (1960).

3. Petitioner also contends (Pet. 4, 8-9) that the Commission acted arbitrarily and denied due process when it entered the revocation order in the present proceeding, and shortly thereafter, in an independent proceeding, substantially reduced sanctions which had been imposed on petitioner by the National Association of Securities Dealers in a disciplinary action in which petitioner had been charged, *inter alia*, with churning in the years 1956 through 1963.[11] This contention is frivolous. In the NASD appeal the Commission held that the question of churning was not properly before the NASD's Board of Governors and that the Board could properly have considered only violations of the extension-of-credit provisions of Regulation T under the Securities Exchange Act. Since the Commission made no determination on the merits of the charges of churning in the NASD proceeding (see Pet. App. 56), its reduction of the penalty in that proceeding is in no way inconsistent with the sanction it imposed in the instant case.

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[11] *Russell L. Irish* (Securities Exchange Act Release No. 7718, October 5, 1965).

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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Securities and Exchange Commission.

JANUARY 1967.

APPENDIX

STATUTES INVOLVED

1. The Securities Act of 1933 (48 Stat. 74, as amended, 15 U.S.C. 77a, *et seq.*) provides in pertinent part:

FRAUDULENT INTERSTATE TRANSACTIONS

SEC. 17. (a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

* * * * * *

2. The Securities Exchange Act of 1934 (48 Stat. 881, as amended, 15 U.S.C. 78a, *et seq.*) provides in pertinent part:

MANIPULATIVE AND DECEPTIVE DEVICES

SECTION 10. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails,

or of any facility of any national securities exchange—

* * * * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

* * * * *

OVER-THE-COUNTER MARKETS

SECTION 15. * * * *

(b) * * * *

(5) The Commission shall, after appropriate notice and opportunity for hearing, by order * * * revoke the registration of, any broker or dealer if it finds that such * * * revocation is in the public interest and that such broker or dealer, whether prior or subsequent to becoming such, or any person associated with such broker or dealer, whether prior or subsequent to becoming so associated—

* * * * *

(D) has willfully violated any provision of the Securities Act of 1933, or of the Investment Advisers Act of 1940, or of the Investment Company Act of 1940, or of this title, or of any rule or regulation under any of such statutes.

* * * * *

(c) (1) No broker or dealer shall make use of the mails or of any means or instrumentality of inter-

state commerce to effect any transaction in, or to induce the purchase or sale of, any security (other than commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange, by means of any manipulative, deceptive, or other fraudulent device or contrivance. The Commission shall, for the purposes of this subsection, by rules and regulations define such devices or contrivances as are manipulative, deceptive, or otherwise fraudulent.

* * * *

SECTION 15A. * * * *

* * * *

(*l*) The Commission is authorized, if such action appears to it to be necessary or appropriate in the public interest or for the protection of investors or to carry out the purposes of this section—

* * * *

(2) after appropriate notice and opportunity for hearing, by order to suspend for a period not exceeding twelve months or to expel from a registered securities association any member thereof, or to suspend for a period not exceeding twelve months or to bar any person from being associated with a member thereof, if the Commission finds that such member or person—

(A) has violated any provision of this title or any rule or regulation thereunder, or has effected any transaction for any other person who, he had reason to believe, was violating with respect to such transaction any provision of this title or any rule or regulation thereunder.

(B) has willfully violated any provision of the Securities Act of 1933, as amended,

or of any rule or regulation thereunder, or has effected any transaction for any other person who, he had reason to believe, was willfully violating with respect to such transaction any provision of such Act or rule or regulation.

* * * *

RULES UNDER THE SECURITIES EXCHANGE ACT OF 1934, 17 CFR 240.0-1, ET SEQ.

* * * *

Rule 10b-5, 17 CFR 240.10b-5. Employment of manipulative and deceptive devices.

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

() To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

* * * *

Rule 15c 1-2, 17 CFR 240.15c 1-2. Fraud and misrepresentation.

(*a*) The term "manipulative, deceptive, or other fraudulent device or contrivance," as used in section 15(c)(1) of the Act, is hereby defined to include any

act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

(*b*) The term "manipulative, deceptive, or other fraudulent device or contrivance," as used in section 15(c)(1) of the Act, is hereby defined to include any untrue statement of a material fact and any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, which statement or omission is made with knowledge or reasonable grounds to believe that it is untrue or misleading.

(*c*) The scope of this section shall not be limited by any specific definitions of the term "manipulative, deceptive, or other fraudulent device or contrivance" contained in other rules adopted pursuant to section 15(c)(1) of the Act.

* * * *

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